IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 76 of 1987

For Approval and Signature:

Hon'ble MR.JUSTICE M.S.SHAH
and
Hon'ble MR.JUSTICE D.A.MEHTA

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : NO

2. To be referred to the Reporter or not? : NO

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the Civil Judge? : NO

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COMMISSIONER OF INCOME TAX

Versus

NANALAL MANSUKHRAM

Appearance:

1. INCOME TAX REFERENCE No. 76 of 1987
MR BB NAIK with MR MANISH R BHATT for Petitioner No. 1
SERVED BY RPAD - (N) for Respondent No. 1

CORAM : MR.JUSTICE M.S.SHAH
and
MR.JUSTICE D.A.MEHTA

Date of decision: 28/08/2001

ORAL JUDGEMENT

(Per : MR.JUSTICE D.A.MEHTA)

The Income Tax Appellate Tribunal Bench `C' has referred the following two questions under sec. 256 (2) of the Income Tax Act, 1961 (hereinafter referred to as `the Act') at the instance of the Revenue:

(i) "Whether, the reasoning of the Appellate Tribunal that the disallowance of interest paid on the amounts received from parties other than partners of the firm under section 40 (b) of the Income Tax Act, 1961 was not justified and hence the orders of the Income Tax Officer and the Appellate Asstt. Commissioner could not be sustained ?"

(ii) "Whether, when both the authorities below had examined all the detailed facts and found that the moneys claimed to have been received for the purpose of the charity were in fact utilised by the firm, the Appellate Tribunal was right in law in interfering with the decision of the lower authorities and directing the deletion of the interest disallowed and added to the income of the assessee ?"

2. The assessment years involved are 1980-81 and 1981-82. The relevant accounting periods are S.Y. 2035 and 2036. The assessee is a private firm and it was maintaining charity accounts known as `Subh Accounts' in its books of accounts in relation to the amounts of money received from various persons who were related to the partners. Admittedly, the assessee was not required to return the funds received from such persons and in view of the said fact, the Income Tax Officer treated the said amounts as capital receipts in hands of the assessee firm. However, in view of the fact that though these moneys were required to be utilised only for charitable purposes and yet were utilised for the purposes of business of the assessee firm, the Income Tax Officer disallowed the interest paid on the balances standing in such accounts. The Appellate Assistant Commissioner confirmed the view adopted by the Income Tax Officer.

3. Being aggrieved, the assessee went in appeal before the Tribunal and the Tribunal for the reasons stated in its order dated 26-7-1985 allowed appeals for both the years.

4. Mr. B.B. Naik, learned counsel appearing on behalf of the applicant- Revenue assailed the order of

the Tribunal mainly on the ground that the funds in question were merely capital receipts in hands of the assessee and that there was no borrowing made by the assessee firm on which it was necessary to pay any interest and hence the assessee could not claim deduction of any such interest paid. It was further contended that in absence of two parties who could enter into a contract, it was a case of the firm paying interest to itself and such interest could not be permitted to be allowed as a deductible item against the taxable income of the firm. It was further contended that the funds in question were admittedly received for the purpose of being utilized for charitable purposes and in spite of that the firm had used the said funds for its own purposes and at the same time paid interest thereupon and claimed deduction of such interest paid which was not permissible.

5. Though served, none has appeared on behalf of the respondent.

6. We find no infirmity in the reasoning of the Tribunal. Section 36 1 (iii) of the Act permits allowance of interest paid on any capital borrowed for the purposes of business. In the present case, it is not in dispute that the funds received by the assessee firm were treated as capital receipts in hands of the assessee firm by the Income Tax Officer. The said funds were utilised for the purpose of business by the assessee and it has paid interest on such funds utilised in its business. The Tribunal has found as a matter of fact that the Revenue has not doubted the genuineness of the stand taken by the assessee in respect of various accounts bearing the character of public trust. In view of this factual situation, once the Department accepts that the monies lying to the credit of various accounts do not belong either to the firm or to its partners but belong to third party and if such funds are utilised for the purpose of business and interest is paid, it has to be held that such interest is rightly claimed as a deductible item of expenditure.

7. The reference by the Tribunal to Section 40 (b) of the Act is only to emphasise the difference in funds being utilized by the assessee. Hence the reference to section 40 (b) in question No.1 is erroneously made and has no relevance to the controversy at hand.

8. We, therefore, hold that on the facts found by the Tribunal, the disallowance of interest paid on the amounts received from various parties other than partners

of the firm was not justified and the Tribunal was right in law in holding it to be so.

9. Both the questions referred to us are therefore answered in the affirmative i.e. in favour of the assessee and against the Revenue.

The Reference is disposed of accordingly with no order as to costs.

(M.S. Shah,J)

(D.A. Mehta,J)

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